

April 22, 2003

Gregory H. Friedman
Inspector General
U.S. Department of Energy
1000 Independence Avenue, S.W.
Washington, DC 20585

Dear Inspector General Friedman:

We are writing to request that you initiate an investigation into recently reported actions by members of the Federal Energy Regulatory Commission (FERC) which may have violated FERC's own regulations regarding off-the-record communications with outside parties. Such communications, if they occurred, raise serious questions about the integrity and fairness of ongoing proceedings involving many millions of dollars of contested electricity contracts entered into by utility companies in the Western U.S. during the California energy crisis and perhaps other pending matters as well.

As reported by the Wall Street Journal on March 28, 2003, FERC Chairman Pat Wood and Commissioner Nora Brownell "held a password-protected conference call with a select group of Wall Street analysts" on or about March 26, 2003 ("Power Points: Second Thoughts on FERC's California D-Day" by Mark Golden) (Attachment I). According to this report, the conference call included a discussion of several cases pending before the Commission involving the abrogation of long-term power supply contracts signed during the California energy crisis; the report further suggests that, in the course of the call, the Commissioners indicated how they expected to vote on these pending matters.

The participation of these Commissioners in the conference call, if as reported, raises serious questions as to whether Commissioners Wood and Brownell complied with the Administrative Procedures Act (APA) and Commission rules. Specifically, Section 557(d) of the APA (5 U.S.C. § 557(d)) provides, in part, that "no member of the body comprising the agency . . . shall make or knowingly cause to be made to any interested person outside the agency an ex parte communication relevant to the merits of the proceeding." In addition, Rule 2201 of the Commission's own Rules of Practice (18 C.F.R. §385.2201), provides, in relevant part, that "in any contested on-the-record proceeding . . . no decisional employee shall make or knowingly cause to be made to any person outside the Commission, any off-the-record communication."

Rule 2201 further provides that where a decisional employee does make a prohibited off-the-record communication, that employee "will promptly submit to the Secretary that communication, if written, or a summary of the substance of that communication, if oral" and that the Secretary shall place that communication or summary in the public file associated with the proceeding. As of this date, there has been no public notice of the Secretary's receipt of a submission about communications in the reported March 26 conference call. Thus, if the FERC commissioners and/or other decisional employees participated in the analysts' call as reported, the requirements set out by the APA and FERC's own rules may have been violated. Motions recently filed with FERC in the cases at issue by the Southern California Water Company and Public Utility District No. 1 of Snohomish County, Washington (Attachment II) and by the California Electricity Oversight Board and California Public Utilities Commission (Attachment

III) raise similar concerns.

In addition to having concerns about possible violations of FERC's own rules, we are also troubled that Chairman Wood and Commissioner Brownell appear to have chosen to provide timely and important information about energy markets and specific companies engaged in those markets only to a select audience of certain Wall Street analysts. One of the fundamental principles underlying the nation's securities laws and financial markets is that all investors should have equal access to basic information about a stock or other security before trading in it.

This is the principle behind a Securities and Exchange Commission rule prohibiting issuers from intentionally disclosing material information to a select few before the general public. Although this rule does not apply to FERC, certainly federal agencies should hold themselves to the highest standard of fairness. In this case, it appears that the FERC Commissioners did not. They instead appear to have provided advance notice of important and relevant information to some market participants (those analysts who were permitted to be on the password-protected conference call) at the expense of others (such as individual shareholders of affected energy companies). We are concerned that such conduct by a federal agency undermines fair and transparent markets.

Finally, we are concerned that Chairman Wood and Commissioner Brownell may have impermissibly prejudged the significant matters pending before them. Under Section 556(b) of the Administrative Procedures Act, administrative proceedings must be "conducted in an impartial manner" (5 U.S.C. § 556(b)), and due process considerations similarly require an impartial decision-maker. To the extent that administrative decision-makers make statements that indicate that they have reached a decision about the facts and law of a particular case before hearing the case, the principle of impartiality has been breached. (See Richard J. Pierce, Jr., Sidney A. Shapiro and Paul R. Verkuil, *Administrative Law and Process* (2nd ed. 1992) at 426-30). The Commission is not scheduled to hear arguments on the first of these cases until tomorrow; other cases are scheduled for oral argument on May 15, 2003. If, as reported, the Commissioners made statements in the conference call on March 26, 2003 about how they were likely to rule on the specific facts of the cases pending before FERC, such conduct may have amounted to impermissible prejudgment of those cases.

At a minimum, we hope you would examine the following questions:

- 1) Whether or not Chairman Wood, Commissioner Brownell or any other FERC employee participated in a conference call with Wall Street analysts on or about March 26, 2003 as reported. (If other employees did participate, their identities and whether they were "decisional employees" should be determined.)
- 2) If such a conference call took place, who were the analysts who participated? How was their participation arranged? How were they chosen? Did any represent companies, or affiliates of companies, that were parties to the pending contract abrogation proceedings or to any other pending FERC proceeding that was discussed or referred to during the conference call?
- 3) Who within FERC participated in setting up and agreeing to these arrangements? Was FERC's General Counsel or other legal advisor consulted in advance of the call with regard to possible conflicts with FERC regulations and practices?

- 4) What specific information was conveyed by each FERC participant? Did any of the information relate to specific cases pending before the Commission? Was any of the information information that had not at the time been provided to the public?
- 5) What were the ground rules or procedures under which the call took place? How was access to the information discussed in the call controlled? What kind of records were kept of the contents of the call?
- 6) Did the participation of FERC commissioners or employees in such a call violate FERC's Rules of Practice, the Administrative Procedures Act, or any other law, rule or regulation either governing communication of federal officials with outside parties or relating to the impartiality of administrative decision-makers?
- 7) Do Commission employees make a practice of holding conference calls or meetings with a select group of participants where information that could affect the financial markets is disclosed? How often has this occurred in the past? What were the circumstances of those calls or meetings? Has anyone ever been denied access? What procedures are there or should there be to govern FERC's disclosure of information that is likely to have an impact on the financial markets?
- 8) Did either Chairman Wood or Commissioner Brownell submit information about the communications made in the conference call to the Secretary of the FERC to be placed in the public files associated with the cases at issue? If so, what was the nature of that submission and when was it provided to the Secretary? If there was such a submission, did it comply with the requirements of Commission Rule 2201?

In the wake of the Western energy crisis, the Enron scandal, and revelations concerning improper practices by some of the nation's leading energy companies such as "round-trip" trading and providing false information to market index publications, it is critical to reestablish investor and consumer confidence in our energy markets. A vigilant, effective, and credible FERC is key to achieving this goal. We hope you agree that the American people, as both consumers and investors, deserve to know whether or not FERC has compromised its regulatory responsibilities in any way.

If you or your staff have any questions concerning this letter, please contact David Berick of Senator Lieberman's staff at 202-224-2627 or Angela Becker-Dippman of Senator Cantwell's staff at 202-224-3441.

Sincerely,

Joseph I. Lieberman
Ranking Member Member
Committee on Governmental Affairs

Maria Cantwell
Committee on Energy and Natural Resources